

## Message Text

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ACTION EB-07

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FM AMEMBASSY KATHMANDU

TO SECSTATE WASHDC 5645

INFO AMEMBASSY NEW DELHI

UNCLAS KATHMANDU 2995

E.O. 11652 N/A

TAGS: EFIN NP

SUBJ: RASTRA BANK CHANGES INTEREST RATE STRUCTURE

1. NEPAL RASTRA BANK ON JULY 9 ANNOUNCED A REVISION OF THE INTEREST RATE STRUCTURE FOR COMMERCIAL BANK TRANSACTIONS EFFECTIVE AS OF JULY 16. DEPOSIT RATES WERE ONLY NOMINALLY REDUCED, WHILE LOAN RATES FOR SELECTED CATEGORIES WERE SUBSTANTIALLY LOWERED IN ORDER TO STIMULATE ACTIVITY IN KEY SECTORS. CHANGES WERE MADE IN THE CONTEXT OF A MUCH IMPROVED MONETARY SITUATION COMPARED WITH LAST YEAR, WHEN A SHARP INCREASE IN RATE STRUCTURE HAD BEEN IMPOSED TO COMBAT INFLATION AND COMMODITY SPECULATION AND TO FOSTER GREATER RESOURCE MOBILIZATION.

2. SPECIFIC CHANGES ARE AS FOLLOWS: RATES FOR SIMPLE SAVINGS, THREE- AND SIX-MONTH TIME DEPOSITS (8, 4 AND 10 PER CENT, RESPECTIVELY) ARE UNCHANGED; ONE-YEAR TIME DEPOSIT RATE DOWN FROM 15 TO 14 PERCENT TWO YEAR FROM 16 TO 15 PER CENT. FIXED-CAPITAL LOAN CHARGES ARE REDUCED FROM 15 TO 10 PER CENT FOR COTTAGE AND RURAL INDUSTRIES AND TO 11 PER CENT FOR "BASIC", IMPORT-SUBSTITUTION, EXPORT, AGRO, AND FOREST-PRODUCT INDUSTRIES; WHILE INCREASED TO 16 PER CENT FOR LUXURY -GOODS INDUSTRIES. LOANS FOR WORKING CAPITAL IN ALL THE ABOVE CATEGORIES WILL BE CHARGED

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AT A 14 PER CENT RATE. IN THE AGRICULTURAL SECTOR, THE

FIXED-CAPITAL LOAN RATE. IN THE AGRICUTURAL SECTOR, THE  
FIXED CAPITAL LOAN RATE FOR PLANTATION CROP VENTURES IS  
REDUCED FROM 10 TO 8 PER CENT; FOR LIVESTOCK, POULTRY,  
FISHERY, SERICULTURE, BEE-RAISING PROJECTS FROM 12  
TO 11 PER CENT; AND FOR OTHER AGRICULTURAL LOANS FROM 15  
TO 14 PERCENT. THE RATE FOR GENERAL COMMERCIAL LOANS  
REMAINS UNCHANGED (I.E., 18 PERCENT, WITH THE EXCEPTION OF  
EXPORT FINANCING, FOR WHICH THE RATE IS 15 PER CENT).

3. COMMENT: WHETHER THE BANKS WILL BE ABLE TO MAKE A  
PROFIT UNDER THE NEW RATE STRUCTURE IS NOT CLEAR. HOWEVER,  
IN THE OVERALL MACRO-ECONOMIC CONTEXT, THE RAJASTHAN BANK MAY  
CONSIDER IT WORTHWHILE TO PROVIDE SUBSIDIES IF NECESSARY TO  
SUPPORT THIS STRUCTURE. WITH THE ABATEMENT OF INFLATION, THE  
NEED TO STIMULATE; YET THE EXCELLENT RESULTS OF LAST YEAR'S DEPOSIT  
RATES INCREASE ARGUED AGAINST A SUBSTANTIAL REDUCTION IN  
THOSE RATES. COMMERCIAL BANK SAVINGS AND TIME DEPOSITS HAD  
INCREASED BY RS. 300 MILLION FROM APRIL 1975 (WHEN  
THE HIGHER DEPOSIT RATES WERE INTRODUCED) TO APRIL 1976,  
AS COMPARED TO A 90 MILLION INCREASE IN THE PREVIOUS ONE-  
YEAR PERIOD. OF EQUAL IMPORTANCE, ALTHOUGH THE CASUAL  
RELATIONSHIP IS NOT DIRECTLY DEMONSTRABLE, INTRODUCTION OF  
THE HIGH RATE STRUCTURE COINCIDED WITH A DRAMATIC  
TURNAROUND IN UNAUTHORIZED CAPITAL FLOWS OUT OF INDIA INTO  
INDIA, THE ERRORS-AND-OMMISSIONS CATEGORY IN INDIA'S INDIAN  
RUPEE PAYMENTS ACCOUNT, WHICH PRIMARILY CONSISTS OF SUCH  
FLOWS, SWUNG FROM A LEVEL OF AROUND NR. 170 MILLION LOSS IN  
FY74/75 (JULY TO JULY) TO A POSITIVE (PROJECTED) LEVEL OF  
RS. 160 MILLION IN FY75/76.

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